

EX PARTE OR LATE FILED

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION
WASHINGTON, D.C. 20554

MAY 11 1994

FCC MAIL ROOM

Amendment of Parts 32 and 64 of the)
Commission's Rules to Account for)
Transactions between Carriers and) CC Docket No. 93-251
Their Nonregulated Affiliates)

MOTION FOR LEAVE TO FILE LATE

Please accept the enclosed late filed comments in the above-captioned docket. Upon initial review of the materials in this docket, we determined that the FCC's proposals were reasonable and did not require comments. However, the attached comments go beyond the FCC's initial proposals. We now believe the comments may be useful to this docket, because they are related to utility/nonutility transactions and regulated/nonregulated cost allocations.

Copies of this motion and the attached comments of the Public Service Commission of Wisconsin are being served on all commenting parties identified in the Commission's records as of January 10, 1994.

Enclosed are the original plus nine copies such that each Commissioner may receive a personal copy.

Dated at Madison, Wisconsin, May 10, 1994.

Respectfully submitted,

Cheryl L. Parrino

Cheryl L. Parrino
Chairman

Public Service Commission
of Wisconsin

cc: William A. Kehoe III
Accounting and Audits Division
2000 L Street, N.W.
Washington, D.C. 20554

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CC Docket No. 93-251

In the Matter of:

Amendment of Parts 32 and 64 of the)
Commission's Rules to Account for)
Transactions between Carriers and) CC Docket No. 93-251
Their Nonregulated Affiliates)

COMMENTS OF
THE PUBLIC SERVICE COMMISSION OF WISCONSIN

Overall, we want to commend the Federal Communications Commission (FCC) in its efforts to supervise transactions with affiliates and proper cost allocations. Generally for each issue raised in this docket, we find the FCC's proposal to be well supported and an improvement over existing rules.

The predominant issue addressed in the proposal was transfer pricing of sales from nonutility affiliates to utilities. The proposal would now limit the use of "prevailing company pricing" such that it can only be used when the unregulated affiliate sells at least 75 percent of its output to non-affiliates. The comments by LECs claiming current rules are adequate is clearly refuted by the recent abuse identified in the FCC staff audit of BellSouth. BellSouth Services achieved excess earnings by overcharging BellSouth telephone companies for its services.

There is a flaw in the LEC's argument that price cap rules remove the incentives to cross-subsidize. Existing cross-subsidies, such as those identified in the BellSouth case, would become embedded in price

caps. These proposed FCC accounting rules will hopefully help to identify such abuses.

The comments included here supplement the proposals in the above-captioned docket, and propose further amendments addressing the same goal as this docket, which is to enhance the FCC's ability to prevent carriers from imposing the costs of nonregulated activities on interstate ratepayers. Overall, we support the existing proposals; however, we feel that they do not go far enough.

Our concerns are organized in the following manner: (1) Pricing of transfers of intangible assets; (2) Allocation of New Product and Systems Development Costs; and (3) Are FCC Part 32 and 64 rules giving results that allocate costs fairly between regulated and nonregulated services?

1. Pricing of transfers of intangible assets

In general, the proposed rules for pricing asset transfers should protect ratepayers from the costs of nonregulated activities. In addition, another important effect of such rules is that such asset transfers also should not cross-subsidize nonutility activities. To protect ratepayers, the proposed rules require a higher of cost or market standard when assets are transferred from the utility to an affiliate, and the lower of cost or market standard when transferred in the opposite direction. However, the concern we raise is that a definition of asset is lacking. We feel that such a definition is needed and should unambiguously include intangible assets.

In today's business environment, numerous business assets are intangible. Even though self created intangible assets may have no book value, the investment community certainly recognizes their worth. Considerable monies are spent on product development and business systems development. This knowledge should be valued at the higher of cost or market if it is transferred to nonutility activities. Currently, it is subject to abuse in that utilities claim no asset has been transferred because costs were expensed as they were incurred. However, the danger is that a significant business advantage would be transferred to the nonutility affiliate free of charge while its competitors must pay to develop such knowledge.

2. Allocation of New Product and Systems Development Costs

Regulators have always struggled with how to allocate new product and system development costs. The above pricing of intangible asset transfers is intended to address when such nonregulated activity is transferred to a structurally separate subsidiary. In addition, the issue needs to be addressed as to how to allocate these costs when the nonregulated activity is not structurally separate. We propose that another cost pool in Part 64 be required. This new product and system development cost pool would include all costs that do not support any current regulated or nonregulated services.

When such developmental work is carried out, it is unknown whether it will create a regulated or a nonregulated product or service. The abuse that occurs is, due to this element of doubt, utilities claim the work is entirely for regulated products. When, after the fact, it

turns out that nonregulated products were developed, there is no mechanism in Part 64 or Part 32 to go back and reallocate those costs. Where plant does have such a true up mechanism, expenses do not. Therefore, this kind of work should be required to be grouped into a separate cost pool. That cost pool should be a shared cost pool. The issue could then be addressed as to what is the appropriate allocation method to use for this shared cost pool.

3. Are FCC Part 32 and 64 rules giving results that allocate costs fairly between regulated and nonregulated services?

Creating any regulatory method involves the statement of the problem, the development of the system to address the problem, the implementation of the system and then reviewing the results of that system to determine its effectiveness and making corrections, if necessary. Improvement is a continuous process. An ongoing evaluation looks at the results of the allocation practices and asks the question, "Do the results reasonably approximate what would be expected?"

As a point of reference, the end results of Part 32 and 64 rules could be compared to such a simple allocation method as using nonregulated versus regulated revenues as an overall basis for allocations. One would expect, in an industry that has so many new products under development, that the allocation to nonregulated activity would be at least as much as would be allocated under a revenue allocator.

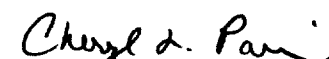
The accounting profession may be a resource to turn to for improvements to cost allocation practices. While we recognize that the

FCC follows GAAP where consistent with regulatory needs in its Part 32 and Part 64 rules, principles developed for unrelated specific circumstances under GAAP may be useful to regulators. For example, the principles of fully allocated costs as developed for segment reporting, while not required to be applied under GAAP to utility regulated versus nonregulated allocations, may be readily applicable and effective. It appears these segment reporting GAAP rules are what the FCC intends to be applied to non-average schedule LECs that are not large enough to file a CAM. The question naturally arises, "How do these two cost allocation methods compare?"

Developing such comparisons will either enhance our confidence in the cost allocation practices or help identify where further refinements are necessary. Please accept these comments as a contribution to the difficult but continuous process of evaluating the allocation of costs between regulated and nonregulated activity.

Dated at Madison, Wisconsin, May 10, 1994.

Respectfully submitted,


Cheryl L. Parrino
Chairman
Public Service Commission of
of Wisconsin

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cc: William A. Kehoe III
Accounting and Audits Division
2000 L Street, N.W.
Washington, D.C. 20554